

CALIFORNIA PUBLIC UTILITIES COMMISSION

May 9, 1997

The Honorable John D. Dingell, Ranking Member
Commerce Committee Democratic Office
564 Ford House Office Building
U.S. House of Representatives
Washington D.C. 20515

Dear Representative Dingell:

Thank you for your letter of April 10, 1996, addressing electric industry restructure issues. Commissioner Conlon has asked me to respond on his behalf. California's state legislature and this commission have been active leaders in this area for several years. In addition to repsonding to the thoughtful questions posed in your letter, I have taken the liberty of attaching copies Commissioner Conlon's March 20, 1997 testimony before the U.S. Senate Energy Committee, copies of A.B. 1890, California's landmark legislation for electric restructure and a copies of the Commission's preferred policy for restructure and the decision on cost recovery plans. In addition, your staff may find our web site, <http://www.cpuc.ca.gov>, an interesting source of current information about electric restructure in progress.

I would be happy to speak with you or any member of your staff at any time. Please don't hesitate to telephone or write for further information.

Sincerely,

A handwritten signature in black ink, reading "Paul Clanon". The signature is fluid and cursive, with the first name "Paul" and last name "Clanon" clearly distinguishable.

Paul Clanon
Energy Division Director

cc Commissioner P. Gregory Conlon.

RESPONSE TO QUESTIONS

1. adoption of retail competition and effect on consumer prices.

California's program will lead to direct access to electric marketers by customers, true retail competition, by January 1, 1998. In order to accomplish our policies we have frozen rates to recover stranded costs over a four year transition. We expect prices to fall - dramatically. We will use the revenues at frozen levels to recover ongoing costs during transition and recover stranded costs. See our cost recovery plan decision for a discussion on "headroom".

2. has your state asked for federal legislation, etc.

No. See in particular my testimony of March 20, 1997. Our preference is for either no federal legislation at this time, or at a minimum, inclusion of a clear "grandfathering" provision for California.

3. does California have sufficient authority to recover stranded costs

Yes. See in particular, A.B. 1890 and the preferred policy decision. California has provided to the utilities a reasonable opportunity to recover stranded costs. Although there is an ongoing proceeding for detailed implementation, see our web site, the cost recovery decision shows the broad scheme.

4. issues surrounding PUCHA and PURPA reform/repeal.

California has no utilities presently affected by PUCHA and we have taken no position on either its reform or repeal. With respect to PURPA, again we have taken no position on either its reform or repeal.

5. constitutional issues

- a) (a) mandated adoption of retail competition.

California would prefer to see reciprocity for energy producers within California to sell to customers in other states. Our desire to reform the state's industry and introduce retail competition was so strong that we pursued a program where out-of-state producers would be able to sell to Californians even without the ability for Californians to sell directly to customers elsewhere. Any federal legislation should only enhance and not retard reciprocity.

- b) state's discretion

California would prefer to see as open a market as possible. If preserving states' discretion not to open their markets would be necessary in order to not interfere with California's program, that would be preferable to federal action which could alter our policies.

6. practical problems of not grandfathering

The question correctly presupposes the fact that a failure to grandfather existing programs in any new federal legislation would impact several states. For California everything from the basic industry structures of power exchanges, independent system operators and direct access as described in

the preferred policy and AB 1890 would be imperiled and our start date of January 1, 1998 would be rendered inoperable. Additionally, our unique plans for cost recovery, see the costs recovery plan decision, would be rendered moot. Ours is uniquely crafted to meet public policy need and economic realities in California, and while we proudly explain it to all who will listen, we do not advocate any California model as the *one-size-fits-all* restructure solution for the rest of the country.

7. protection of small and residential customers

An integral element of all of California's restructure was the public policy conclusion that the small and residential customers should not be harmed as a result of larger customers' use of political or market power. California has only approved rate discount "anti-bypass" contracts where there has been a positive contribution to costs and not a cost-shift to other customers. In fact we have been working towards a policy of pricing electricity at the "marginal costs" and have been gradually reducing rate subsidies which were embedded in rates from prior generations of policy decisions.

8. recent rate trends

Rates in California, as distinct from costs, have been held stable in recent years. In fact an integral foundation to our cost recovery plan is to use the revenue which results from frozen rates and falling costs to fund the recovery of stranded utility assets. As discussed above, our recent rate design decisions have been predicated on eliminating non-cost-related pricing differentials between customers.

9. sale of generation facilities and elimination of retail rate regulation

As fully described in our preferred policy, California envisions an electric services industry with three major components: an unregulated fully competitive generation/energy market, a federally rate regulated transmission market with fair and open access (as embodied in FERC Order 888), and state rate regulated distribution services. It is our belief that that marketplace is the best price setter for competitive energy/commodity and that performance-based incentive regulation is the preferred alternative for monopolistic services including the transmission and distribution of electricity. This system will lead to the correct allocation of benefits.

10. reciprocity

See our comments above and testimony of March 20th. Reciprocity is preferable, and only federal legislation or adoption of an inter-state compact can provide it. But, we would forgo it if legislation would either alter or delay California's program

11. unbundling distribution

We believe that unbundling is a necessary component of electric restructure. See our preferred policy and the ongoing proceedings described in our web-site.

12. public power and federal power issues

A.B. 1890 provided for specific incentives and authority for public power in California to participate in the industry restructure proposed by this commission. These provisions should eliminate or reduce most concerns over any unfair advantages or protections enjoyed by public power. Federal marketing entities such as WAPA present their own unique issues concerning the risk of anti-

competitive marketing practices by tax-subsidized federal power projects competing with investor-owned power. Federal action

13. funding needs of a near-term date certain

California requires no extra funding from state or federal sources to implement its own or a federally mandated electric restructure.

14. securitization of stranded asset recovery

A.B. 2890 provides for a vehicle to use "rate reduction bonds" to recover costs allocated to residential and small commercial customers. If properly structured, these bonds should have a very high rating for security and our aim is for a "AAA" rating; this provides a significant savings over utility financing costs at a "A" rating. The revenue stream from customers will secure the bonds. The customers will have a fixed and limited liability. We believe this will work for California.

15. PUCHA Reform

The Commission and the state of California have not taken a position on PUCHA reform.